

# DEFENSE CONTRACT MANAGEMENT COMMAND

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## Progress Payment Analysis

### Analyst Refresher Training

**Robert C. Monico**  
**SFA-Pricing**

**201-393-2032**  
**rmonico@dcmde.dla.mil**

# **Progress Payment Analysis**

## **Analyst Refresher Training**

**Risk-based Approach Statement:** This presentation will discuss various areas of the analysis of progress payments. The depth and scope of any particular review should be based on regulatory requirements in the context of a risk-based management environment.

# **Progress Payment Analysis**

## **Training Objectives**

- Identify & Describe Process Inputs
- Discuss Accounting, Regulatory & Contractual Framework of Analysis
- Detail Analysis Process & Techniques
- Mention Proposed Policy Changes

# **Progress Payment Analysis**

## **Process Inputs Identified- 1**

- Price/Cost Analysis or Review Request (DLA Form 1542)
- Progress Payment Administration Record (DLA Form 325)
- Contractor's Request for Progress Payment (Standard Form 1443)
- Audit Report - Accounting System (DCAA)

# **Progress Payment Analysis**

## **Process Inputs Identified - 2**

- Disclosure Statement
- Post-award Financial Surveillance Report (DLA Form 1530)
- Physical Progress Report
- Supporting Documentation or
- Audit Report - Progress Payment (DCAA)

# **Process Inputs Described**

## **Price/Cost Analysis or Review Request (DLA Form 1542)**

- ACO Initiated
- Timing of Review
  - Pre-payment (Higher Risk/Priority)
  - Post-payment (Lower Risk/Priority)
- Specific ACO Concerns

# **Process Inputs Described**

## **Progress Payment Administration Record (DLA Form 325)**

- Accounting System Status? (FAR 32.503-3)
- Payment/Liquidation Rates? (DFARS 252.232-7004)
- First Article Approval? (FAR 52.209-3, ALT II)
- First Article Limitation Set? (FAR 32.501-5)

# **Process Inputs Described**

## **Contractor's Request for Progress Payment (Standard Form 1443)**

- Cost-based Payment
- SF 1443 Required (FAR 32.503-1)
- Frequency: Once a Month (FAR 52.232-16)
- Suspension/Reduction for Fraud (FAR 32.006)
- Subject to False Claims Act/Mail Fraud Statute



# Process Inputs Described

## Audit Report - Accounting System: 1

- Adequate Accounting System/Controls (FAR 32.503-3)
- System Review within 12 Months (FAR 32.503-3)
- DCAA Audit Codes
  - “17740” Pre-award Accounting System Survey
  - “26000” Accounting System & Controls (CPFF,FPIF,etc.)
  - “11070” Accounting System & Controls (FFP only)

# Process Inputs Described

## Audit Report - Accounting System: 2

- System Description - A
  - Accounting Period?
  - Basis for Booking Costs (i.e. accrual)?
  - Frequency of Posting to General Ledger?
  - Frequency of Financial Statements?

# Process Inputs Described

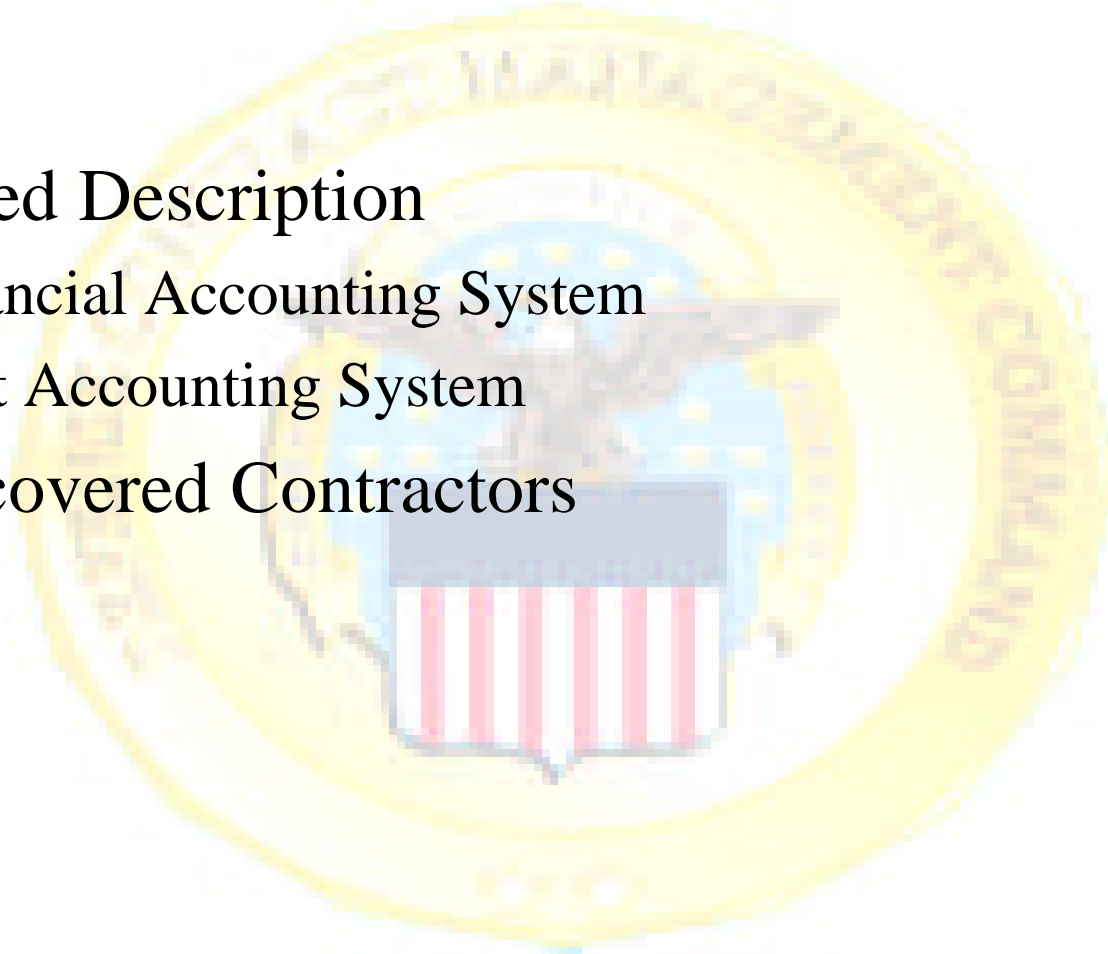
## Audit Report - Accounting System: 3

- System Description - B
  - Job Cost Accounting System?
  - Indirect Cost Pools & Allocation Bases?
  - Recording of Indirect Expenses & Billing to Projects?
  - Direct & Indirect Cost Charging Practices?

# Process Inputs Described

## Disclosure Statement

- Detailed Description
  - Financial Accounting System
  - Cost Accounting System
- CAS-covered Contractors



# **Process Inputs Described**

## **Post-award Financial Surveillance Report (DLA Form 1530) - 1**

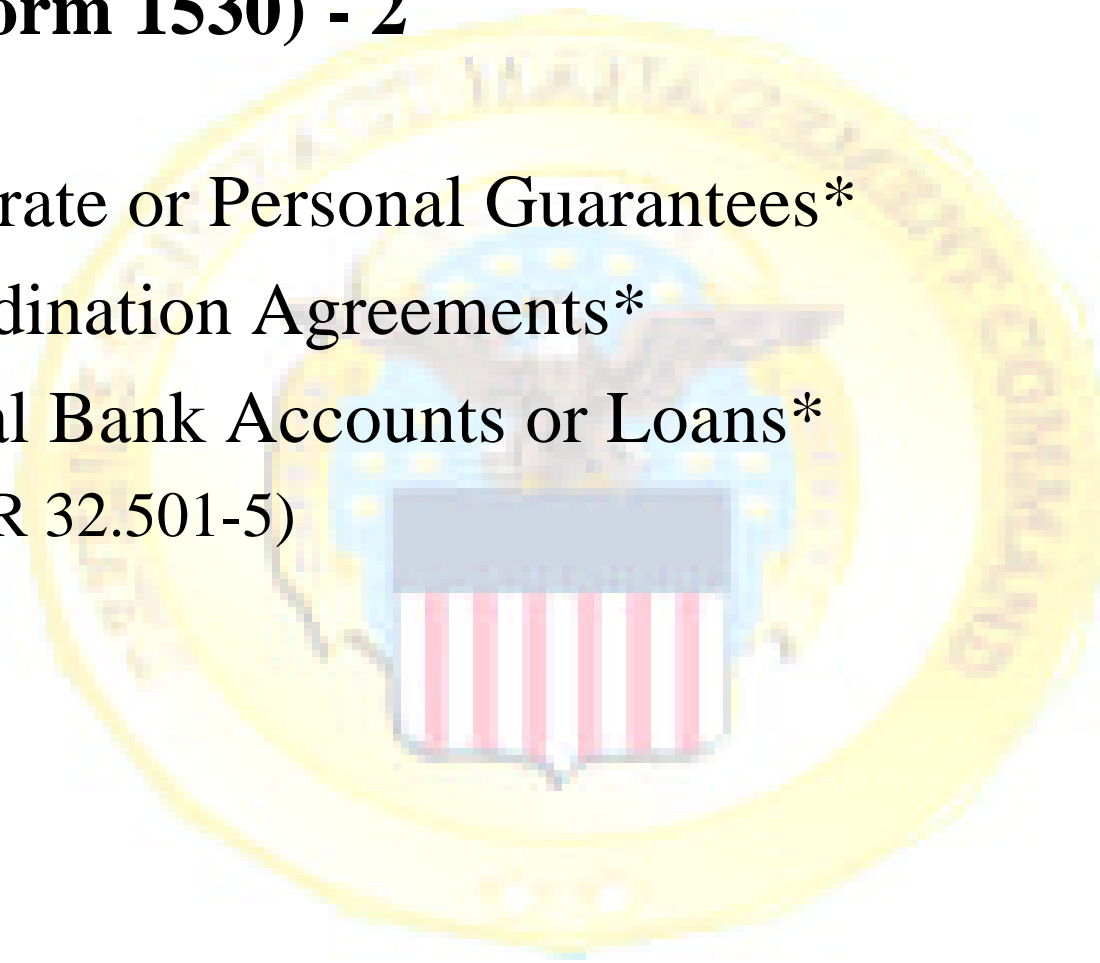
- Annual Financial Statements
  - Balance Sheet
  - Income Statement
  - Cash-flow Statement
- Financial Analysis
- Dun & Bradstreet Reports

# **Process Inputs Described**

## **Post-award Financial Surveillance Report (DLA Form 1530) - 2**

- Corporate or Personal Guarantees\*
- Subordination Agreements\*
- Special Bank Accounts or Loans\*

\* (FAR 32.501-5)



# Process Inputs Described

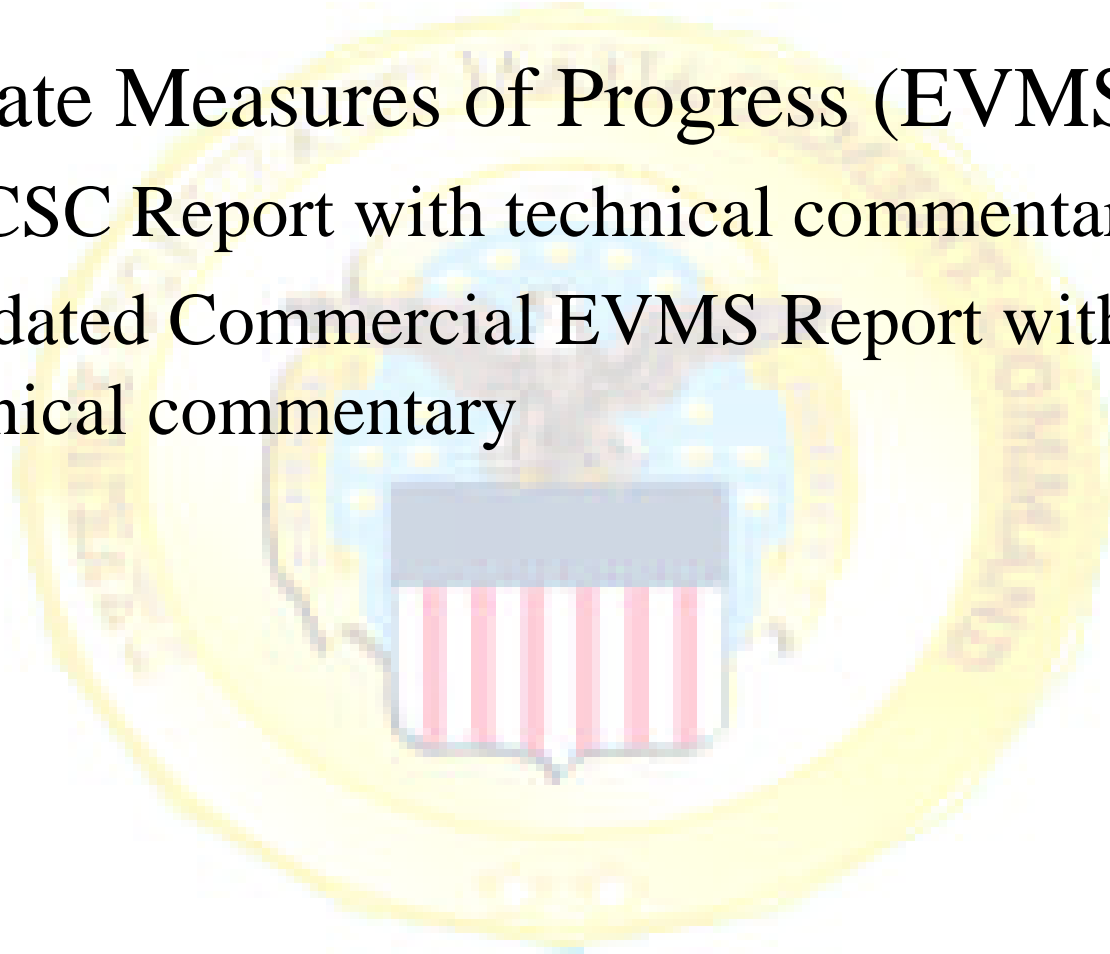
## Physical Progress Report - 1

- Weighted Value Progress Payment Chart (DLA Form 1503)
  - Performance Element Summary Sheets (Form 1503a)
- Percentage of Physical Completion
  - Added Value Method, Weighted Value Technique
- Technical Analysis of Contractor's ETC

# Process Inputs Described

## Physical Progress Report - 2

- Alternate Measures of Progress (EVMS)
  - C/SCSC Report with technical commentary
  - Validated Commercial EVMS Report with technical commentary

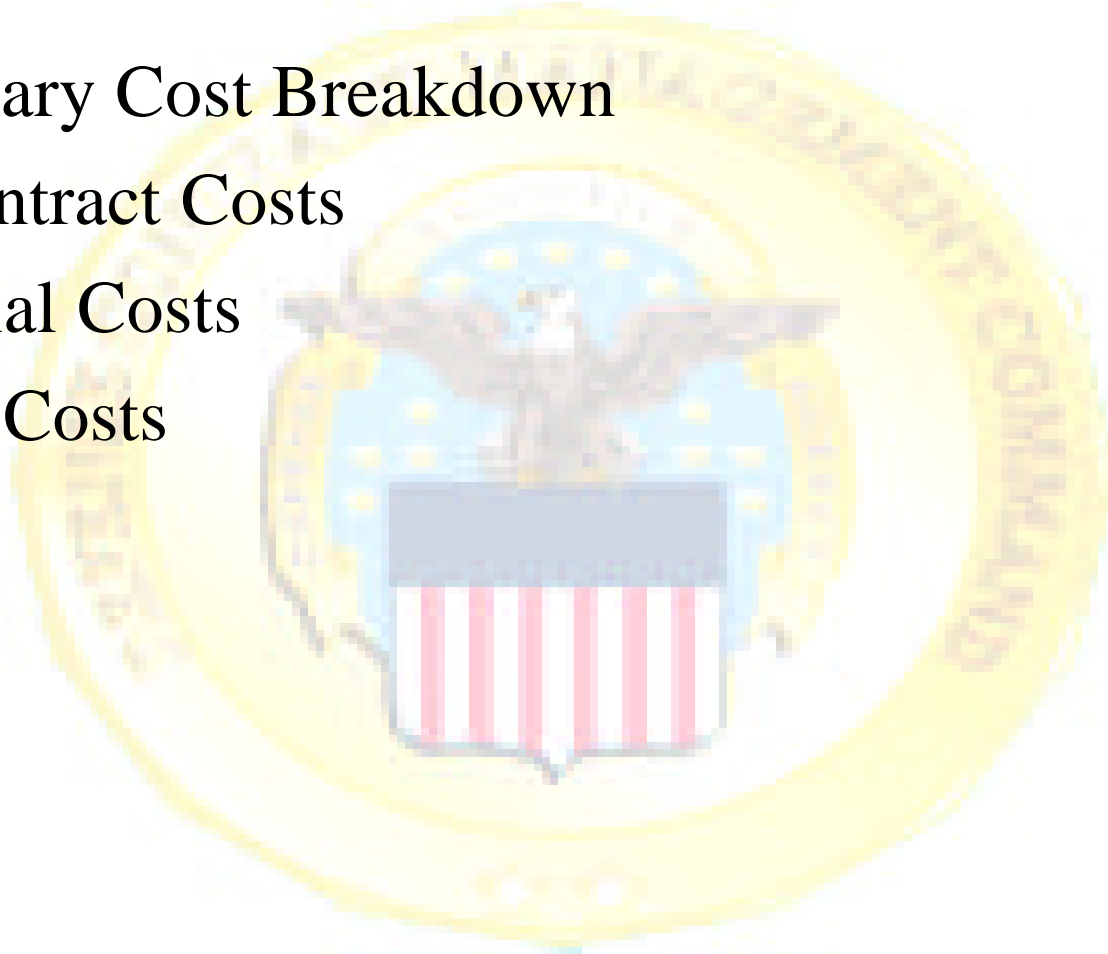




# Process Inputs Described

## Supporting Documentation - 1

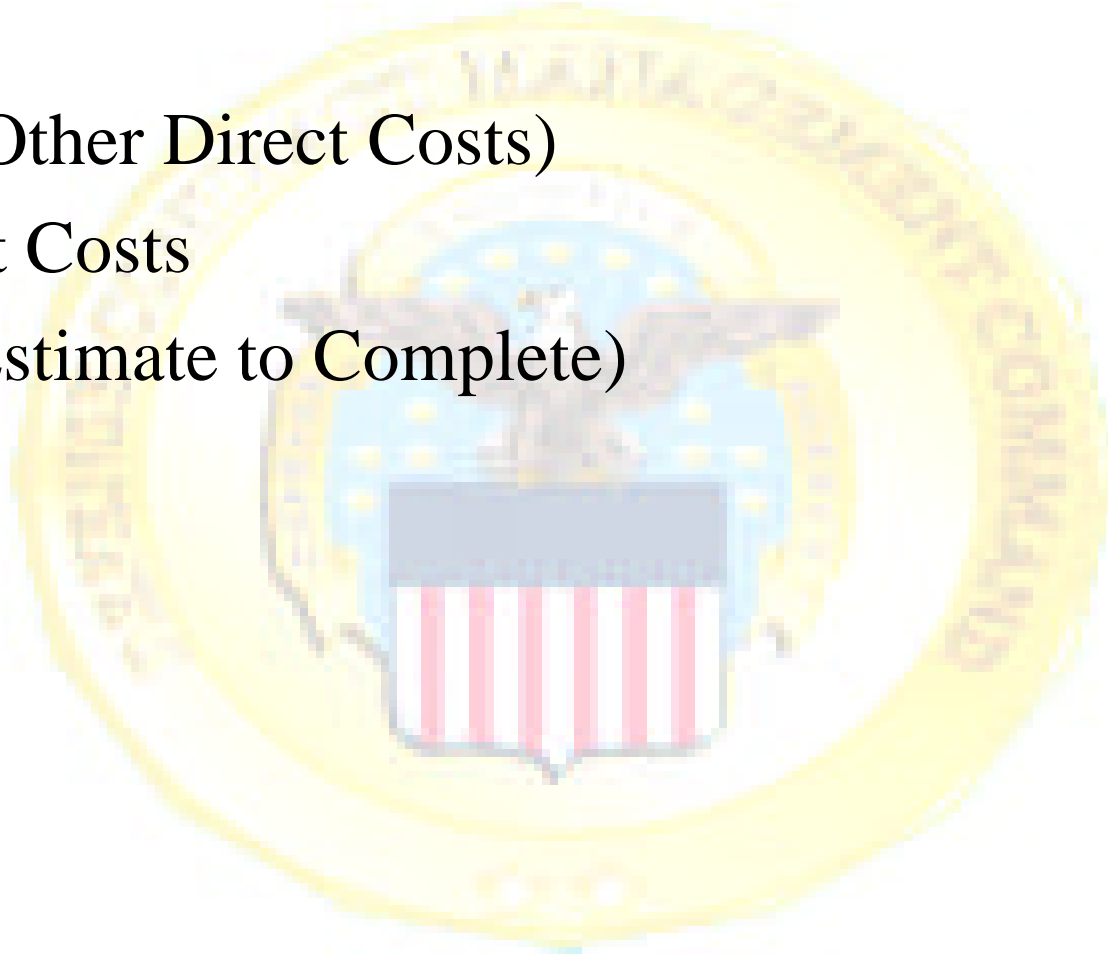
- Summary Cost Breakdown
- Subcontract Costs
- Material Costs
- Labor Costs



# Process Inputs Described

## Supporting Documentation - 2

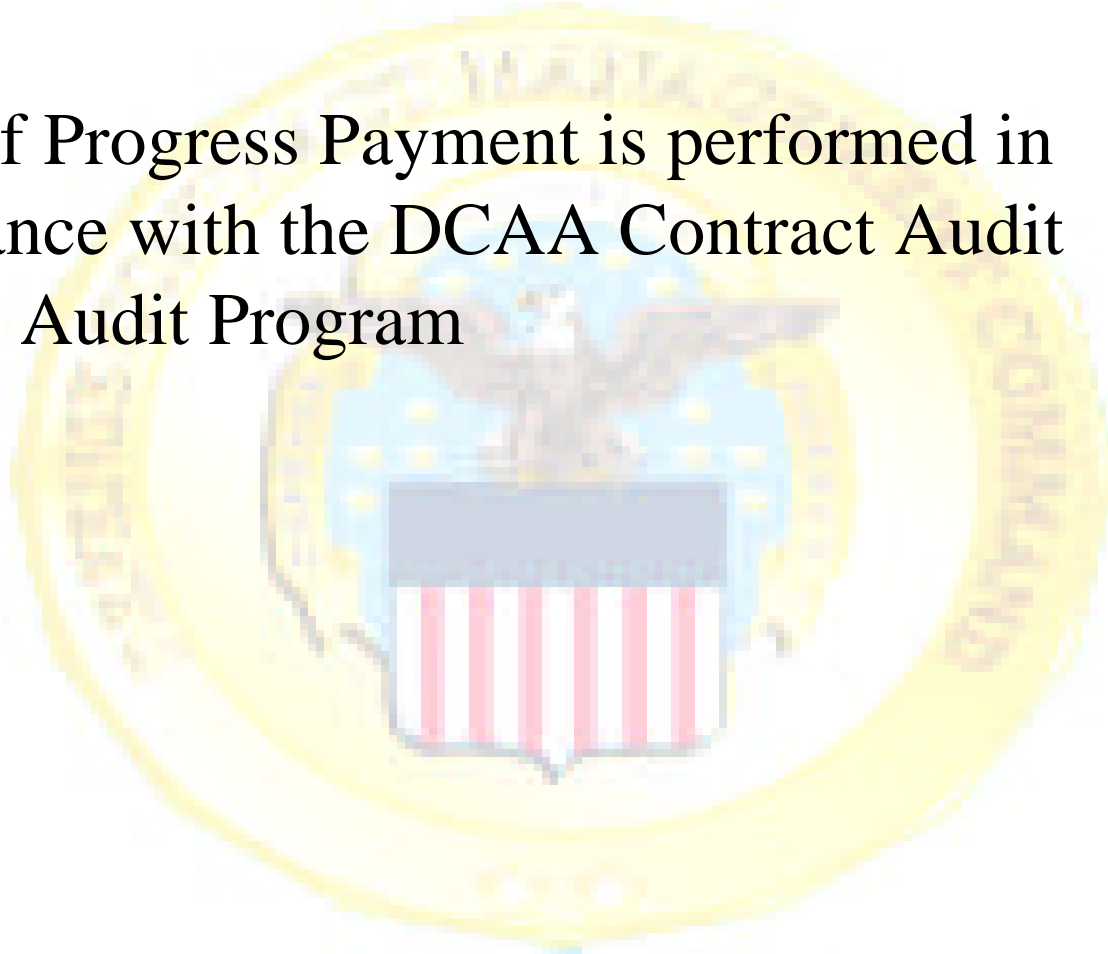
- ODC (Other Direct Costs)
- Indirect Costs
- ETC (Estimate to Complete)



# **Process Inputs Described**

## **Audit Report - Progress Payment**

- Audit of Progress Payment is performed in accordance with the DCAA Contract Audit Manual Audit Program



# Regulatory & Contractual Framework of Analysis

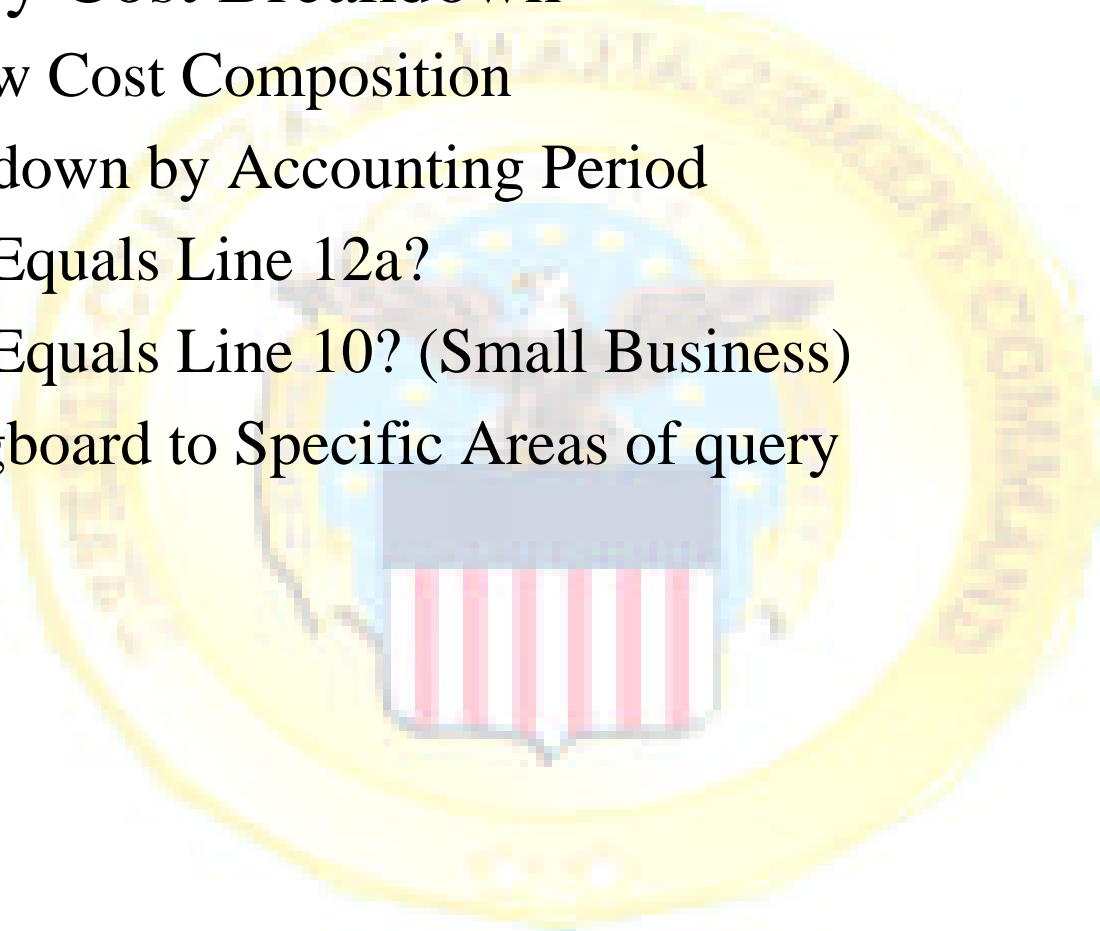
- Accounting Practice
  - GAAP
  - CAS
- Allowability (FAR 31)
  - Expressly Unallowable (i.e. contingency costs)
  - Allocable (i.e. common hardware charged direct)
  - Reasonable (i.e. commercial item from affiliate)

# Regulatory & Contractual Framework of Analysis

- Paid v.s. Incurred Costs (FAR 52.232-16)
  - Paid costs only for large business
  - Incurred costs for small business
- Title Requirement (FAR 52.232-16)
  - Contractor must have obtained title to item
- First Article Approval
  - Allocable (FAR 52.209-3 or -4)
  - Limitation (FAR 32.501-5)

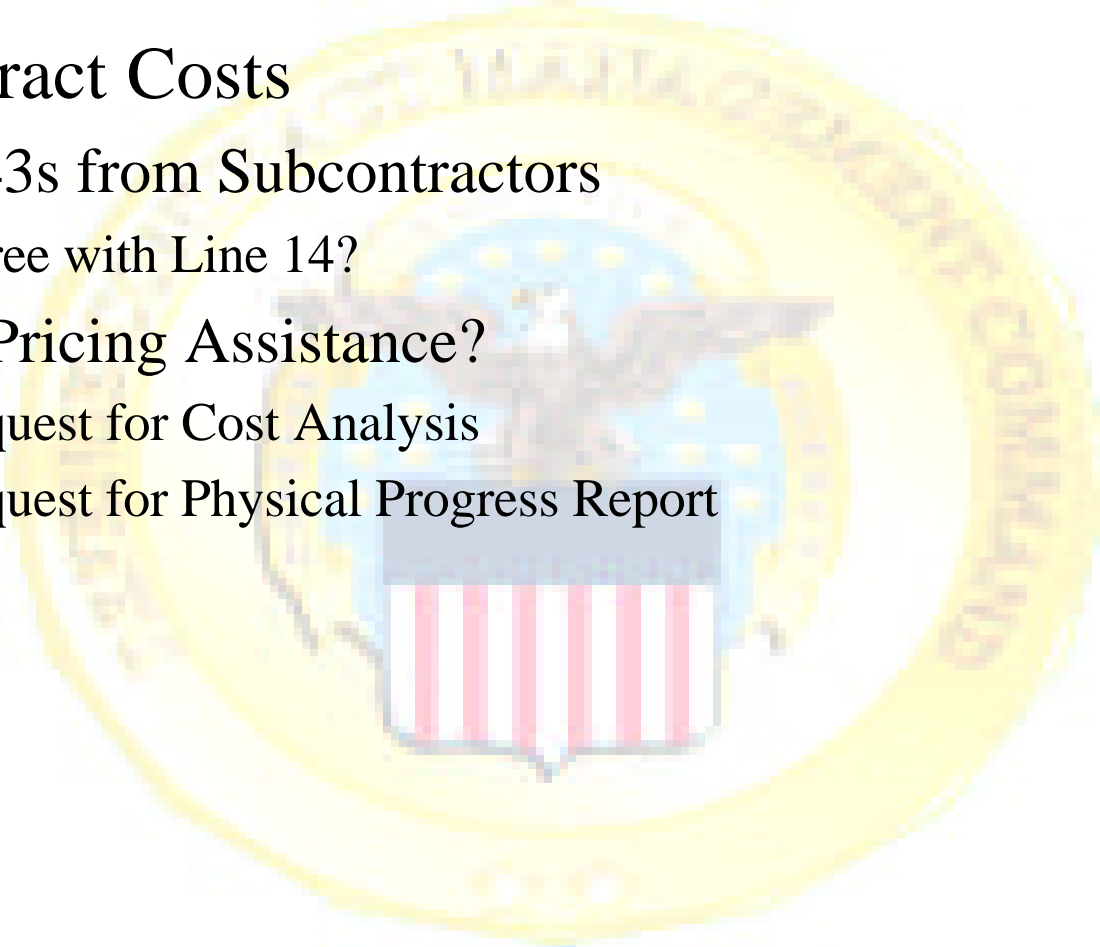
# Analysis Process

- Summary Cost Breakdown
  - Review Cost Composition
  - Breakdown by Accounting Period
  - Total Equals Line 12a?
  - Total Equals Line 10? (Small Business)
  - Springboard to Specific Areas of query



# Analysis Process

- Subcontract Costs
  - SF1443s from Subcontractors
    - Agree with Line 14?
  - Field Pricing Assistance?
    - Request for Cost Analysis
    - Request for Physical Progress Report



# Analysis Process

## Material Cost Analysis - 1

- Material Cost Report
  - Equals Amount on Summary Cost Breakdown?
  - Composition of Costs?
    - Purchased Parts/Material
    - Inter-divisional transfers
    - Issued from stock
    - Work in-process (WIP)



# **Analysis Process**

## **Material Cost Analysis - 2**

- Composition
  - Allocable in Terms of Kind
  - Allocable to First Article
- Purchased Material/Parts
  - Date Incurred? (Invoices Dates)
  - Date Title Obtained? (Shipment Dates)
  - Advanced Payments?
    - Bilateral Subcontract with FAR 52 Clause Required

# Analysis Process

## Material Cost Analysis - 3

- Inter-divisional Transfers
  - Profit Pyramiding Prohibited (FAR 31.205-26)
  - Beware of Commercial Item Pricing
- Issued From Stock
  - Prior Make or Buy?
  - Method of Establishing Cost?

# Analysis Process

## Labor Cost Analysis

- Labor Cost Report
  - Equals Amount on Summary Cost Breakdown
  - Composition of Costs? (Mfg; Assy & Test; Eng)
  - Date Labor Paid/Accrued
  - Exempt Personnel Charged Direct & Indirect
  - Allocability
    - Labor Classification
    - First Article Allocable

# **Analysis Process**

## **Other Direct Cost**

- Travel Costs (FAR 31.205-46)
- Consultant Costs (FAR 31.205-33)
- Special Tooling & Test Equipment (FAR 31.205-40)

# **Analysis Process**

## **Indirect Costs Analysis**

- DCAA Audited Rates?
- ACO Billing Rates?
- FPRA/FPRR rates?
- Adjusted for YTD Actuals?

# **Analysis Process**

## **Audit Report - Progress Payment**

- DCAA's Audit Program includes the Administration of the Clause in Terms of the Title Requirement
- Requests for Audit Reports May Address this Important Contractual Requirement

# Analysis Process & Techniques

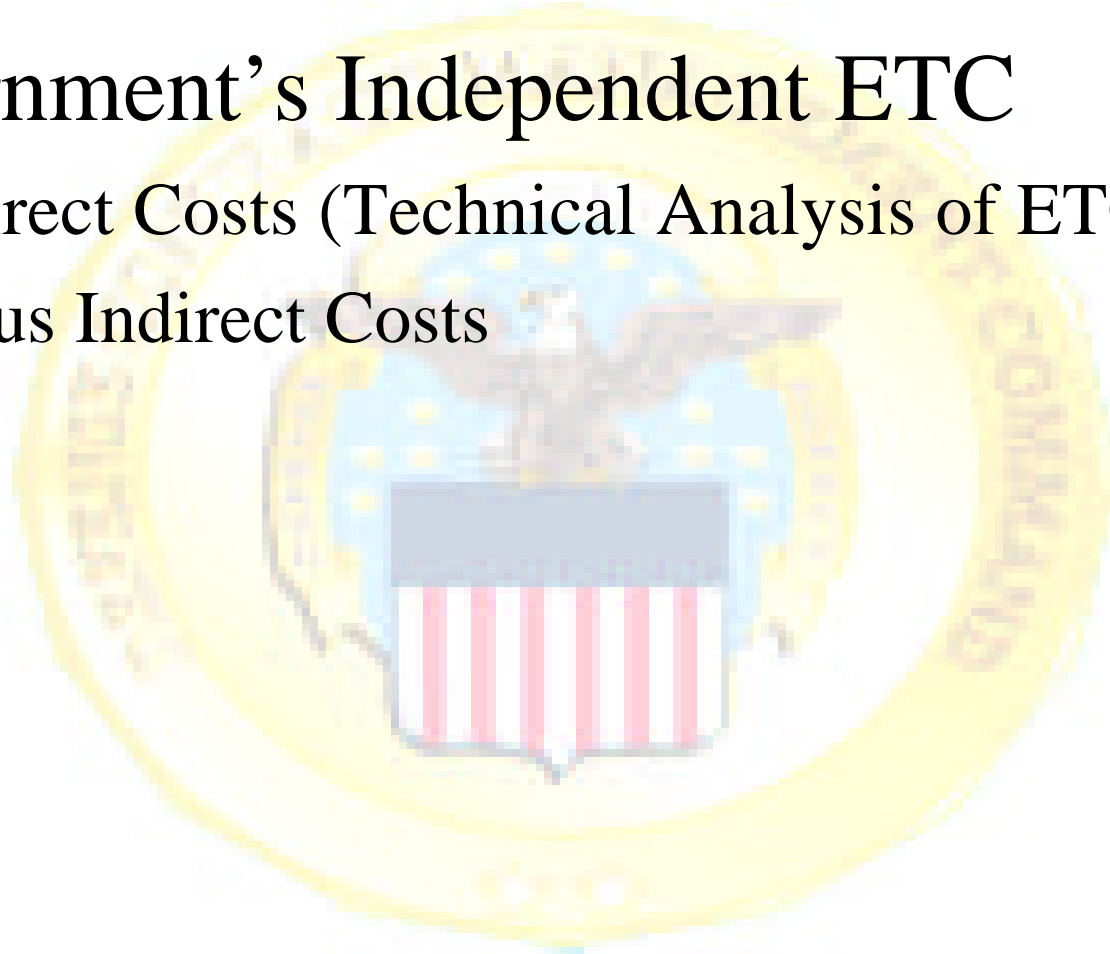
## Estimate To Complete (ETC)

- Contractor's ETC
  - Revise every 6 mos. (SF1443 Instructions)
  - Review Technical Analysis of ETC
  - $IC + ETC = EAC$  (On Revised ETC Date)
  - $EAC - IC = ETC$  (Used for Next 5 Months)

# **Analysis Process & Techniques**

## **Estimate To Complete (ETC)**

- **Government's Independent ETC**
  - Direct Costs (Technical Analysis of ETC)
  - Plus Indirect Costs





# Analysis Process & Techniques

## Estimate At Completion (EAC)

- Government's Independent EAC

- IC + Independent ETC = EAC

- Proportion Method



The diagram illustrates the Proportion Method for calculating EAC. It features a large, faint background image of the Department of Defense seal. Overlaid on this is a smaller shield-shaped graphic with a blue top half and a red and white striped bottom half. The top half of the shield is labeled 'IC' (Incurred Cost). A horizontal dashed line separates the top half from the bottom half, and the bottom half is labeled '% Complete'. To the right of the shield, there is an equals sign followed by a fraction. The numerator of the fraction is 'X' and the denominator is '100%'.

$$\frac{\text{IC}}{\% \text{ Complete}} = \frac{X}{100\%}$$

$$X = \text{EAC}$$

# Analysis Process & Techniques

## Loss Ratio & Application

$$\frac{\text{Contract Price}}{\text{EAC}} = < 1.0 \text{ (Loss Ratio)}$$

Apply to Line 11, Complete Normal Calculations

# Analysis Process & Techniques

## Fair Value Test

- Fair Value of Undelivered Work
  - FV > Unliquidated Progress (FAR52.232-1)
  - Payments Collateral for Government “Loan”



# Analysis Process & Techniques

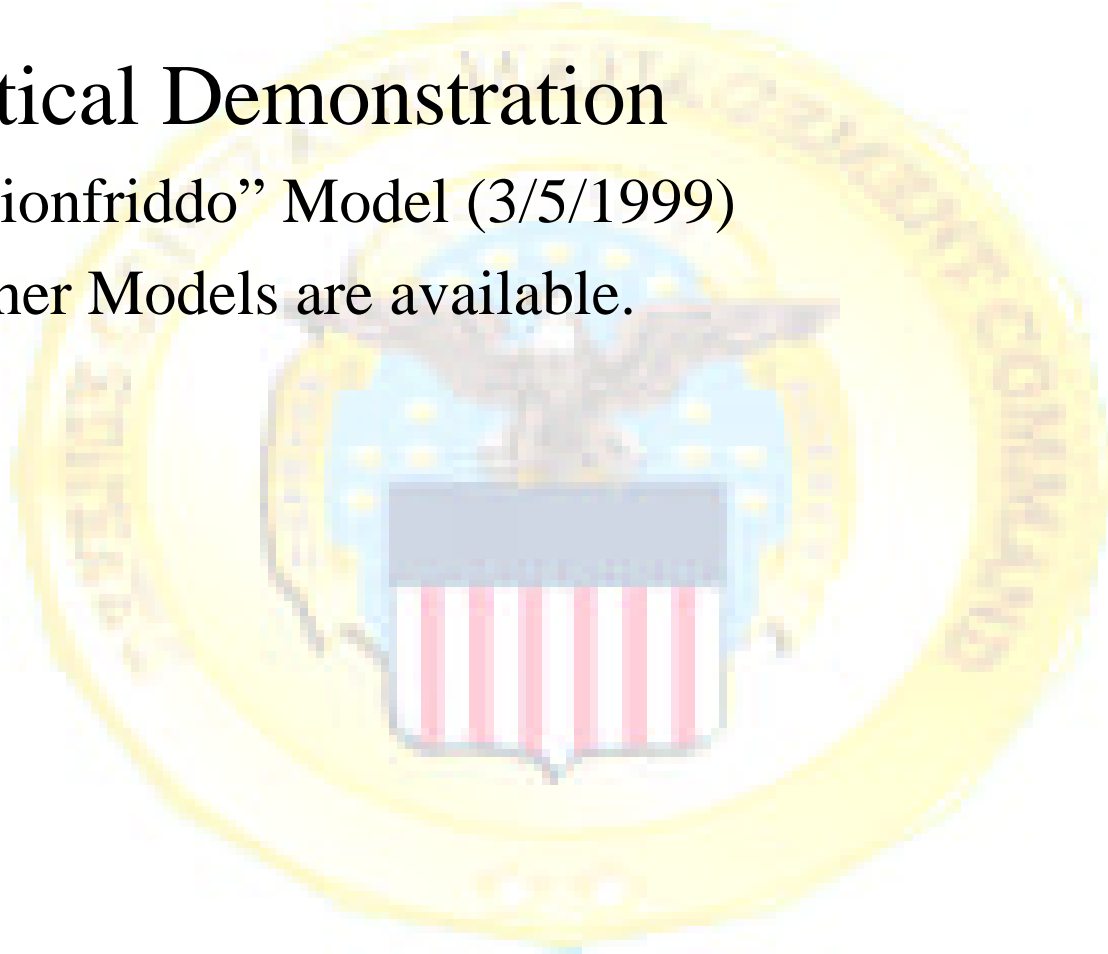
## Fair Value Test

- Fair Value Defined (FAR 32.503-6)
  - Price of Undelivered Work - ETC = FV or
  - IC of Undelivered Work + 20c (14e) = FV
- Unliquidated Progress Payments include Instant Progress Payment Amount

# Analysis Process & Techniques

## Review Models

- Practical Demonstration
  - “Gionfriddo” Model (3/5/1999)
  - Other Models are available.



# Proposed Policy Changes

- Federal Register, February 10, 1999
  - Increase threshold from \$1M to \$2M for LB
  - Establish \$2,500 minimum per payment
  - Eliminate “Paid Cost Rule” for Large Business
  - Emphasize preference for Performance-Based Payments over Progress Payments
  - Permit subcontract PBPs/Commercial Financing

# **Progress Payment Analysis Analyst Refresher Training**

- Additional Comments or Questions
- Thank You for Your Attention!